Preparing for a strong post-COVID growth

A keynote by Himino Ryozo, Commissioner of the JFSA, at the 2020 IIF annual membership meeting on October 12, 2020.

Every week, in the morning of Tuesday and Friday, I have a 30-minute video meeting with the CEO of one of the 102 regional banks in Japan. Each meeting enlightens me on the developments in regional economies and is among the most productive 30 minutes in my day.

Recent series of meetings have made me believe that, although we continue to face highly challenging economic environment, COVID-19 is also creating new opportunities for growth across Japan.

A fitness gym in Ehime prefecture lost a significant number of its members due to the fear of infection but increased its sales by introducing an exercise program remotely guided by a reputed instructor in Tokyo through a video screen and a camera.

In Kamakura, an old city south of Tokyo, demands for apartments are booming. If you work from home four days a week and report to an office in Tokyo once a week, Kamakura provides nice balance between good living environment and reasonable commuting burden. In Saitama and Chiba, demands for single family home are booming due to a similar reason.

The demands for paper for office use have significantly declined, but the demands for paper towel are surging. The demands from high-end restaurants for *Wagyu* beef are stalled, but the demands for *Wagyu* for family dinners compensate the loss. The *Wagyu* beef production was 10

percent lower in April than the year before but 10 percent higher in August.

The COVID shock is unprecedented: It affects both life and economy, it affects both supply and demand, and it affects the whole world. We are still faced with an unprecedented level of uncertainty. But compared with the first half of this year, we know more about what COVID means to us. And as I have just described, sprouts of post-COVID growth are already appearing all around Japan, and the same should be the case for the whole world.

Of course, the current priorities in financial sector policies are securing continued funding to the economy, preventing the recurrence of liquidity panic, ensuring operational resilience, and preparing for any solvency phase of the crisis to come.

Nevertheless, I believe we should also think ahead now how we can best secure a strong post-COVID recovery. There are intertemporal trade-offs for any policy measures. If we look through the various phases in the pandemic cycle and consider immediate and longer-term effects of measures, we should be able to make a better and timelier choice. These are also issues that we are discussing at international level in the FSB Standing Committee on Supervisory and Regulatory Cooperation.

The priority during the liquidity phase of the crisis is securing bridge financing to the corporate sector and to prevent bankruptcies resulting from cash shortage. At an early phase of the pandemic, we do not know which company will be affected to what extent and how long, and thus we cannot distinguish between viable and non-viable firms.

But as more is known about the pandemic and its effects,

banks and borrowers should start thinking about how to meet the challenges of the post-COVID era. If borrowers start addressing the challenges earlier, they will be less haunted by debt overhang. The post-COVID growth will then be stronger.

As the pandemic shock subsides, policy makers will start moving toward exit from emergency measures. We should be mindful of the risk of taking strong medicine for too long. At the same time, policy makers should also be careful about the risk of premature lifting and of the cliff arising from the cumulative effects of the unwinding of multiple measures.

This is a matter of delicate balance. In Japan, we do not want to see tightened lending standard now. Although many surveys in Europe and the United States show recent tightening in bank lending standards, the Bank of Japan's *Tankan* survey indicates that large, medium and small companies of manufacturing and non-manufacturing industries all responded that banks' lending attitudes were as easy in September as in June. We are satisfied with this result.

The Japanese non-financial corporate sector entered the COVID crisis with the lowest level of leverage and the highest level of cash on their balance sheets as seen in the last quarter century. But if the effects of the pandemic should linger on, significant subset of it will face the need to cut costs, find new ways to raise revenues, and restructure their balance sheets. Without necessary restructuring, the economy will not be able to put an end to the legacy of COVID era and transit to the post-COVID growth.

Even if an effective vaccine or cure is developed, many of the changes triggered by the pandemic will stay, and some of

them may even be accelerated. Such changes may include:

- Shifts from face-to-face, on-site services to remote and mobile ones,
- Shifts from paper to digital, including shifts from cash to digital payments,
- For some products and services, shifts towards more globalized markets, where winners take all, and for other products and services, shifts towards more localization,
- Shifts in emphasis from efficiency to resilience, including in the design of supply chains,
- Shifts from the single center city to the network of multiple core cities, and
- Shifts from the city center to suburbs.

Many players will have to design post-COVID business models to lead such changes and to survive in the new environment. The speed and the flexibility in the transformation will probably dictate the strength of the post-COVID growth.

The financial sector has important roles in supporting and facilitating the restructuring and the transformation.

For smaller enterprises, banks will have to play a central role. But this time, the number of borrowers requiring restructuring or transformation could be enormous. The types of supports they require will be diverse, as the problems they face will differ from company to company. Finding solutions to numerous and diverse problems will be a formidable task. At the same time, this would be an opportunity for bankers to show their true values to their customers and the society.

The JFSA is encouraging bankers to liaise with other players in the regional economy. For example, SME Business

Rehabilitation Support Co-operatives, which were established in all prefectures in Japan in 2003, provide advice to small and medium size enterprises (SMEs) and conduct initial discussion with lenders without charging fees to the SMEs. If the SMEs so wish, the co-operatives prepare restructuring plans, coordinate with lenders, and support implementation of the plans.

Some of Japan’s existing banking regulations, particularly the regulations on the scope of business, may be unduly constraining banks’ ability to use their human resources, accumulated information, and network to support borrower restructuring and transformation. Last month, the Minister for Financial Services, Mr. Aso Taro, requested the Financial System Council, an advisory board to the JFSA, to review such regulations.

For the restructuring and transformation of both SMEs and larger companies, the capital markets should play a greater role than before. Last month, Minister Aso also requested the Financial System Council to revisit regulatory frameworks so that the capital market would be able to support sustainable growth in the post-COVID era.

The JFSA and the Tokyo Stock Exchange introduced Japan’s first corporate governance code in 2015 and revised it in 2018. We plan to embark on the second revision, and aim to find what improvements in the code could help listed companies lead the transformation in the post-COVID world and build a sustainable business models.

The Japanese government aims to enhance attractiveness of Japan as an international financial center and considers reforms to attain the aim as a priority policy project.

The JFSA plans to introduce an option for asset managers to be supervised in English from applications to start business in Japan to daily regulatory interactions. The JFSA has submitted requests to the Ministry of Finance to review certain specific features in the Japanese corporate, income, and inheritance tax systems. The JFSA is coordinating with relevant ministries and agencies so that immigration and other policies could also be revisited.

While having a single center in one time zone is the most efficient form of financial service production, that is like putting all eggs in one basket. Given the growing geopolitical, pandemic, and other risks, market participants may consider building resilience through geographical diversification. Making Japan as a good alternative will help build resilience in the regional and global financial system.

And making the Japanese market more oriented towards the world outside Japan is what Japan itself needs now. Building a strong post-COVID growth through a shift to the new social, economic, and industry models is an exercise to be pursued by the whole world. Japan needs to find its post-COVID path by contributing to this joint endeavor.

Thank you.